Title: The Securitisation Regulations 2024	De minimis assessment
SI (Statutory Instrument) No: 2024/102	**Date: 21/11/2023**
Other departments or agencies: None	**Type of regulation: Domestic**
Contact for enquiries: Shiphrah Dixon, Zia Shakeel, Green and Prudential Team, HMT	**Date measure comes into force:** 30/06/2024
Cost of Preferred (or more likely) Option Under £5m	**Equivalent Annual Net Direct Cost to Business per year** (EANDCB in 2022 prices) - None

1. What is the problem under consideration? Why is government intervention necessary?

The Financial Services and Markets Act 2023 (FSMA 2023) repeals retained EU law relating to financial services. This enables the government to deliver a Smarter Regulatory Framework (SRF) for financial services. Retained EU law will be replaced with rules set by our independent and expert regulators, operating within a framework set by government and Parliament. This instrument replaces retained EU law in relation to the UK Securitisation Regulation (Sec Reg) that is revoked by FSMA 2023, with a new regulatory framework tailored to the UK.

As a result of this instrument and the revocation of the retained EU law by FSMA 2023, the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) will be able to make rules that replace existing provisions in retained EU law.

Securitisation is the process of pooling various exposures to form a financial instrument that can be marketed to investors. This packaging allows lenders (such as banks) to transfer the risks of loans or assets (such as mortgages, auto loans, or consumer loans) to other banks or investors. This process can help to reduce lenders' liabilities, which in turn facilitates their further lending to the real economy.

Securitisation activity in the UK is currently primarily regulated by the Sec Reg – the retained UK version of the EU Securitisation Regulation.

The Sec Reg aimed to strengthen the legislative framework for securitisations after the Global Financial Crisis and to revive high-quality securitisation markets.

HM Treasury conducted a review of the Sec Reg in 2021 ('Sec Reg Review'[1]). This fulfilled a legal obligation to review several areas of the regulation. HM Treasury identified a number of areas where reforms could usefully be considered to ensure the regime is as effective as it can be.

The Sec Reg Review aimed to bolster UK securitisation standards to enhance investor protection and promote market transparency, and to support and develop UK securitisation markets to increase their contribution to the real economy.

This SI establishes a new legislative framework for the regulation of securitisation. This instrument does this by using powers in FSMA 2023 to establish new provisions on securitisation by restating (with amendments) some provisions of retained EU law. The instrument also exercises powers in the Financial Services and Markets Act 2000 (FSMA 2000) so as to give the FCA new rule-making powers while also allowing both the FCA and the PRA to exercise their existing rule-making powers.

[1] 2021 Review: https://assets.publishing.service.gov.uk/media/61b370f38fa8f503816404eb/Securitisation_Regulation_Review.pdf

This SI also implements certain reforms identified by the Sec Reg Review and gives the FCA and the PRA powers to restate most firm-facing provisions related to securitisation. HM Treasury are committed to working with the PRA and the FCA to bring forward, where appropriate, policy changes in these areas identified in the Sec Reg Review.

2. What are the policy objectives and the intended effects?

The policy objective is to establish the FSMA model of regulation for the Sec Reg where the financial services regulators generally take responsibility for setting the firm-facing regulatory requirements which are currently set out in retained EU law, acting within a framework set by government and Parliament.

Delivering these reforms under the SRF will provide the UK's securitisation framework with a foundation from which the regulators can make future improvements more agilely, in response to changing conditions, new business opportunities, and emerging risks.

Alongside establishing the FSMA model of regulation, this legislation also implements some of the outcomes of the Sec Reg Review, such as scoping certain non-UK Alternate Investment Fund Managers (AIFMs) out of being subject to UK due diligence requirements. This will ensure more appropriate scope and proportionality for these firms when investing in UK securitisations.

Laying this SI allows HM Treasury and the regulators to rationalise other less substantial elements of the regulation that were not identified in the Sec Reg Review but will nevertheless benefit market functioning, such as renaming the process for Third Party Verification (TPV) 'authorisation' to 'registration' in line with registration for Securitisation Repositories (SRs), to distinguishing it from general FCA and PRA authorisation.

This new legislative framework also sets the perimeter for the regulation of securitisation by introducing powers for the FCA to make firm-facing rules for unauthorised firms under the Designated Activities Regime (DAR) and giving the FCA a corresponding power of direction to ensure they can effectively supervise unauthorised firms for these activities. All providers of securitisations, including firms who are not authorised by the FCA or PRA, are currently subject to requirements in the Sec Reg, and so this maintains the scope of the regulation.

This SI makes other perimeter-setting reform, such as scoping non-UK AIFMs out of UK due diligence requirements as mentioned above. This SI also delegates the supervision of providing securitisations by Occupational Pension Schemes (OPS) to the FCA, in line with its wider remit to supervise these requirements for other firms.

This SI makes other changes to ensure the effective functioning of securitisation under the SRF. This includes modifying HM Treasury's existing power to recognise STS-equivalent non-UK securitisations in line with these regulations, under a refreshed 'overseas simple, transparent and standardised securitisations regime', and requiring the FCA and PRA to 'have regard' to the coherence of the overall framework for the regulation of securitisation when making rules for different firms.

3. What policy options have been considered, including any alternatives to regulation? Please justify preferred option

[Option 1] Do nothing – do not replace retained EU law
The government could choose not to make any replacement legislation when the relevant REUL is repealed. This would result in a regulatory gap, which would pose risks that the Sec Reg seeks to address. These risks could include not requiring manufacturers to retain a net economic interest in securitisations they issue, which could incentivise them to securitise and market riskier assets. Additionally, without appropriate due diligence requirements for institutional investors, they could invest in riskier securitisations which could pose prudential, market, and conduct risks to the UK's financial stability.

This SI enables all providers of securitisations – including those who are unauthorised – to be subject to the regulation of securitisation, by giving the FCA powers to make rules for and supervise unauthorised firms under the Designated Activities Regulation (DAR). If this SI did not provide the FCA with these powers, unauthorised providers of securitisations would remain unregulated, which could pose risks to the UK's financial stability.

Other jurisdictional scope-related reforms, such as narrowing the definition of institutional investor to scope out non-UK Alternative Fund Investment Manager (AIFMs) and clarifying the prohibition on establishing Securitisation Special Purpose Entities (SSPEs), would not be enacted without this SI. Without these changes, overseas AIFMs could be disincentivised from marketing their funds to UK investors and allowing SSPEs in high-risk or jurisdictions to be used in UK securitisations could pose risks to UK financial stability.

Finally, without requiring the FCA and PRA to have regard to the coherence of their rules, which can only be imposed via legislation, there could be an increased risk that the regulation of securitisation could become more fractured and complex for different sets of firms.

[Option 2] Retain EU Law – continue existing EU Law

While REUL is repealed by FSMA 2023, the government could put in place equivalent legislation in order to maintain the status quo for firms. This would not be an appropriate option as it would not be in line with the FSMA model, and so detailed technical provisions which apply to firms would remain in statute. That means the rules which govern the UK's regulation of securitisation would not benefit from the expertise of our operationally independent regulators, and there would be limited opportunity to tailor these rules to the UK. This would also not achieve the government's ambitions for agile rulemaking or the removal of EU law from the statute book, and so these provisions would also be less able to keep pace with international developments and changing market practices. This would ultimately impact the international competitiveness of the UK's financial services sector.

[Option 3] Preferred option – replace retained EU law with legislation tailored to the UK in line with the FSMA model

The preferred option is to commence the repeal of REUL as it relates to rules around securitisation and replace it with legislation tailored to the UK in line with the FSMA model. This will enable the move to the FSMA model of regulation. The FSMA model has been adapted over the years and remains the most appropriate way to regulate financial services in the UK. It ensures that the regulators' day-to-day experience of supervising financial services firms is central to the regulatory policymaking process. It also provides flexibility for the regulators to update standards efficiently in response to changing market conditions and emerging risks.

This instrument exercises the power in section 4 of FSMA 2023[2] to restate provisions from retained EU law with modifications. This instrument also exercises the powers in Part 5A of FSMA 2000[3] to give the FCA new rule-making powers in relation to securitisation.

Additionally, this SI takes forward legislative reforms not present in the current REUL, such as making due diligence requirements for non-UK AIFMs more proportionate, clarifying requirements relating to the establishment of SSPEs, standardising processes for Third Party Verifier and Securitisation Repository registration, and the repeal of monitoring requirements for the FCA and PRA which are duplicative to their statutory objectives. These legislative reforms will make the UK's securitisation framework more robust and improve market functioning.

4. Please justify why the net impacts (i.e., net costs or benefits) to business will be less than £5 million a year.

When REUL is repealed, the detailed rules which apply to firms in relation to securitisation will be replaced with rules set by the PRA and FCA within a framework set by government and Parliament. The PRA and FCA are operationally independent and the impact of these rules on firms will be their responsibility.

Where final impacts are dependent on the outcome of policy decisions which sit within the remit of the independent financial services regulators, HMT is content that in such cases, the regulators have appropriate mechanisms to consider the impact of such decisions. FSMA 2000 requires the regulators to produce cost-benefit analyses (CBA) when they consult on proposed rules. Through FSMA 2023, the government has acted to strengthen this process by requiring the FCA and the PRA to set up panels dedicated to supporting the development and production of the CBA. In future, the regulators will be required to consult these panels on the CBA before they consult publicly on proposed rules.

It is not possible for HM Treasury to pre-judge the rules that the financial services regulators make given the regulators are operationally independent of government. HM Treasury has therefore assessed the direct impact of replacement legislation on firms, rather than any rules that may be made by the regulators in the future.

Until REUL is repealed, provisions in REUL still apply, and firms are required to follow these REUL provisions. Only where HM Treasury's replacement legislation changes the effect of those provisions will there be any impact on firms.

- *What will businesses have to do differently?*

The main impacts on UK firms are likely to be familiarisation costs.[4] This is because this SI does not have any direct firm-facing impacts – instead, it sets the perimeter within which the FCA and PRA can make rules, with these rules directly impacting firms. As above, HM Treasury is unable to pre-judge the rules that the financial services regulators make given they are operationally independent of government.

[2] Financial Services & Markets Act 2023: https://www.legislation.gov.uk/ukpga/2023/29/contents/enacted
[3] Financial Services & Markets Act 2000: https://www.legislation.gov.uk/ukpga/2000/8/contents
[4] There may be additional impacts on non-UK AIFMs as they will be scoped out of the Sec Reg. However, we are primarily interested in how these reforms will affect UK firms, so we have not quantified the costs of these changes for overseas firms.

Firms are, however, likely to engage lawyers or consultants to understand the legislation and accompanying guidance. HM Treasury calculates familiarisation costs as an approximation of the time spent reading the instrument on the basis of the word length of the instrument, the difficulty of the text based on the Flesch Reading Score and the hourly rate of an external legal expert that a business may procure to read the instrument for its business.

- How many businesses will this impact per year?

Numbers of firms affected

The range of UK securitisation originators is broad, with many regular issuers. The public data for non-CLO (Collateralised Loan Obligation) securitisations includes over 130 different originators including non-bank lenders of auto-loans, mortgages, and consumer loans, and banks. Additionally, there are approximately 80 CLO managers in the UK.

The number of affected firms for which there is publicly available information is shown in Table 2 below. The total number of firms here is an upper estimate as some originator firms may act as servicers.

Table: Publicly available UK securitisation data

Firms	**Number**
Originator/sponsor - dual regulated (with the PRA)	62
Originators/sponsor - solo regulated (FCA only)	45
Originators/sponsor – unregulated	24
Originators/sponsor (CLO managers)	80
Total originators/sponsors	**211**
Total servicers	**128 non-CLO UK securitisations**
Total firms (originators/sponsors + servicers)	**339**

Source: Bloomberg/Dealogic/FCA – UK securitisations since 2010[5]

We are unable to estimate the number of firms that invest in securitisations (the 'buy-side'). There are thousands of institutional investors in the UK that invest in diversified portfolios that include various financial products. As such, surveying all these investors to determine which of them invested in securitisations would have gone beyond what was proportionate to the impacts of the changes being proposed.

Institutional investors that may invest in securitisation includes various types of buy-side funds and firms, including AIFMs, Undertakings for Collective Investment in Transferable Securities (UCITS), UCITS management companies, and insurers. However, this SI maintains the scope of which UK buy-side firms securitisation rules apply to, so it is unlikely that FCA and PRA authorised institutional investors will need to incur significant costs to understanding this legislation. Instead, these firms are more likely to invest resource into understanding corresponding regulator rules.

[5] FCA consultation paper on Securitisation rules (August 2023): https://www.fca.org.uk/publication/consultation/cp23-17.pdf

- What is the direct cost/benefit per business per year?

Number of words in SI (rounded up to nearest 100)	Words read per minute	Hourly rate (£)	Number of businesses affected	Familiarisation costs per firm (£) (rounded to 2 significant figures)	Total familiarisation costs (£) (rounded to 2 significant figures)
19800	100	385	339	1271	430669

Note of methodology: We have based the cost of this legal advice on the government guidelines on solicitors' hourly rates, using an hourly rate of £385, based on the following assumptions:

a. As legal expertise in financial services resides predominantly among City law firms, we have used a London, rather than UK-wide value for legal costs.
b. As this work will be undertaken by a variety of individuals with varying levels of experience at different firms, therefore we have used the middle range value for a Solicitor/Associate with 2-5 years' experience.

It is assumed that, as legal experts, readers will generally be familiar with this type of literature, so we have taken the upper bound of the reading speed of difficult text, i.e., 100 words per minute. Furthermore, it is assumed that this form of familiarisation will be undertaken on a one-off basis. These assumptions are the same as the approach that HM Treasury took in its assessment of impact of financial services-related SIs made under the European Union (Withdrawal) Act.

Benefits

It is not possible to quantify the ongoing benefits of the changes made by this SI as benefits will be decided by the approach taken by the FCA and PRA to their respective rules, which the government is unable to pre-judge. However, the government expects the repeal of REUL and its replacement with a new framework that is tailored to the UK will benefit firms in several ways.

In particular, firms will benefit from the more proportionate approach that will stem from replacing detailed EU provisions which were designed to apply across the EU with rules set by the UK's expert and independent regulators. Beyond this, replacing REUL will enable firms to benefit from a streamlined and accessible legislative framework for financial services, where rules adapt over time in an agile manner and in response to changing practices.

5. Please confirm whether your measure could be subject to call-in by BRE (Better Regulation Executive) under the following criteria. If yes, please provide a justification of why a full impact assessment is not appropriate:

a) **Significant distributional impacts (such as significant transfers between different businesses or sectors)**
No
b) **Disproportionate burdens on micro, small, and medium businesses (below 500 employees).**
No
c) **Significant gross effects despite small net impacts**
No
d) **Significant wider social, environmental, financial or economic impacts**
No

e) Significant novel or contentious elements
No

<u>Sign-off for de minimis assessment: SCS</u>

I have read the de minimis assessment and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

SCS of [Policy team]

Signed: ***Fayyaz Muneer*** Date: 17/11/2023

SCS of Better Regulation Unit

Signed: ***Philip Witcherly*** Date: 20/11/2023

<u>Sign-off for de minimis assessment: Minister</u>

I have read the de minimis assessment and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

(Name, Ministerial role)

Signed: ***Bim Afolami, Economic Secretary to the Treasury*** Date: 23/11/2023

Further information sheet

Please provide additional evidence in subsequent sheets, as required.